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In the Supreme Court of the United States

OCTOBER TERM, 1977

IKE SLODOV, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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OPINIONS BELOW

The opinions of the bankruptcy judge (Pet. App. A22-A42) and the district court (Pet. App. A13-A20) are not officially reported. The opinion of the court of appeals (Pet. App. A1-A12) is reported at 552 F. 2d 159.

JURISDICTION

The judgment of the court of appeals was entered on April 5, 1977. The petition for a writ of certiorari was filed on June 23, 1977. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether petitioner is personally liable for the unpaid withholding tax liabilities of three of his corporations, pursuant to Section 6672 of the Internal Revenue Code of 1954.

STATUTES INVOLVED

The pertinent provisions of Sections 6672 and 7501 of the Internal Revenue Code of 1954 (26 U.S.C.) are set forth at pp. 3-4 of the petition.

STATEMENT

On January 31, 1969, petitioner purchased the stock of three corporations, Tas-Tee Catering, Tas-Tee Vending and the Charles Corporation. Petitioner was in control of these corporations from January 31, 1969, through July 15, 1969, except for the two-week period from May 23, 1969, through June 4, 1969 (Pet. App. A2).

During the purchase negotiations, it was represented to petitioner that Tas-Tee had sufficient funds to pay all of its taxes and creditors. On February 1, 1969, petitioner sent to the Internal Revenue Service the corporations' Federal Insurance Contributions Act and withholding tax returns for the last quarter of 1968 and Tas-Tee Catering's returns for the second quarter of 1968. These returns were accompanied by checks totaling $262,705 for payment of the liabilities (Pet. App. A2; Govt. Ex. 6). On February 3, 1969, petitioner discovered that there were not sufficient funds available to cover the checks and he immediately stopped payment on them (Pet. App. A2).

Deposits were made into the corporate checking accounts during the week of February 3, 1969, so that from February 6, 1969, throught February 9, 1969, the balance in the accounts ranged between $130,000 and $150,000 (Joint Ex. 3). While under petitioner's control, the corporations continued to have current operating receipts totaling or exceeding $100,000 per week. Petitioner used these funds in part to pay some of the outstanding employment taxes due the government. However, it is undisputed that petitioner used the remaining part of

the funds to pay employees, rent, utilities and other creditors. Petitioner also reimbursed himself for several advances he had made to the corporations (R. 20, 57; Tr. 179, 181, 239, 348-349, 403-407).[1]

Subsequently petitioner entered into a proceeding for a Real Property Arrangement under Chapter XII of the Bankruptcy Act. The Internal Revenue Service filed a claim for $313,295 owed under assessments made pursuant to Section 6672 of the Internal Revenue Code of 1954 for the second and fourth quarters of 1968 and the first through third quarters of 1969. The bankruptcy judge found that petitioner was not responsible for the collection of withholding taxes until February 1, 1969 (Pet. App. A34). While he further found that petitioner was the person responsible for the collection of such taxes from February 1 to July 15, 1969, he concluded that petitioner's failure to withhold and pay over taxes was not willful within the meaning of Section 6672. He therefore concluded that petitioner was not liable for any of his corporations' unpaid withholding tax liabilities (Pet. App. A37).

The district court reversed the bankruptcy court in part. It ruled that petitioner was personally liable under Section 6672 for the unpaid withholding taxes only for the period after February 1, 1969 (Pet. App. A17-A19).

The court of appeals reversed. It held that petitioner was liable for the unpaid withholding taxes for the period prior to January 31, 1969, but not for the period after that date. It rejected petitioner's argument that he could not be the person responsible for the collection of such taxes prior to the time that he took over control of the corporations

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[1] "R." and "Tr." respectively refer to the record appendix filed in the court of appeals and the trial transcript.

because there were no unencumbered corporate funds on hand at that time. As the court of appeals stated, "When the corporation came into possession of funds after * * * [petitioner] acquired control, these funds were impressed with a trust to the extent of the corporation's obligations for previously unpaid withholding income taxes and employees' share of social security taxes. Though created before * * * [petitioner's] control of the corporation began, these obligations continued after that date, and he was clearly the person responsible for paying them when funds became available" (Pet. App. A11).

ARGUMENT

1. Sections 3102(a) and 3402(a) and (d) of the Internal Revenue Code of 1954, as amended, require every employer to withhold federal income and social security taxes from the wages of his employees. Section 7501 provides that the withheld taxes constitute a special trust fund in favor of the United States. See *Newsome* v. *United States*, 431 F. 2d 742 (C.A. 5). If an employer withholds a tax but fails to pay it over to the United States, the employee is nevertheless credited with having paid the tax and the government will not require any additional payment from the employee. Thus, unless the government has recourse against the person responsible for the collection of the tax, the revenues would be put in jeopardy. *Dillard* v. *Patterson*, 326 F. 2d 302 (C.A. 5).

Section 6672 of the Code gives the government the necessary recourse against the responsible collection officers. It provides that "Any person required to collect * * * and pay over any tax * * * who willfully fails to * * * pay over such tax, * * * shall, in addition to other penalties provided by law, be liable to a penalty equal to the total amount of the tax evaded, or not collected, or not accounted for and paid over." The thrust of the statute is to

impose personal liability upon those persons whose conduct resulted in the failure to pay withheld taxes. *E.g.*, *Mueller* v. *Nixon*, 470 F. 2d 1348 (C.A. 6); *Spivak* v. *United States*, 370 F. 2d 612 (C.A. 2). In the typical case, as here, the statute is used as a collection device against officers of a bankrupt corporation for the taxes withheld from its employees' wages. See, *e.g.*, *Monday* v. *United States*, 421 F. 2d 1210, 1214-1215 (C.A. 7), certiorari denied, 400 U.S. 821; *Gefen* v. *United States*, 400 F. 2d 476, 482 (C.A. 5), certiorari denied, 393 U.S. 1119; *Hewitt* v. *United States*, 377 F. 2d 921, 924 (C.A. 5); *Burack* v. *United States*, 461 F. 2d 1282, 1285 (Ct. Cl.).

The court of appeals correctly held that petitioner was personally liable under Section 6672 for the unpaid taxes withheld prior to his assumption of control of the corporations. As the court stated (Pet. App. A11), "We conclude that it is irrelevant whether there were unencumbered funds on hand at the time * * * [petitioner] took control of Tas-Tee Catering. Prior to that time the employees of the corporation had received net wages which reflected withholding for income taxes and social security taxes." When petitioner took over the corporation which thereafter came into possession of funds, these funds were impressed with a trust to the extent of the corporation's unpaid withholding tax liabilities. Since petitioner was aware of the unpaid taxes and possessed the power and responsibility to pay them, his preference of other corporate creditors over the government rendered him liable for the tax under Section 6672. See *Braden* v. *United States*, 442 F. 2d 342, 344 (C.A. 6), certiorari denied *sub nom. Bonistall* v. *Braden*, 404 U.S. 912; *Teel* v. *United States*, 529 F. 2d 903 (C.A. 9). Accord: *Stake* v. *United States*, 347 F. Supp. 823 (D. Minn.); *Louisville Credit Men's Assn, Inc.* v. *United States*, decided September 29, 1970, 73-2 U.S.T.C. par. 9740 (E.D. Ky.).

2. Contrary to petitioner's argument (Pet. 7), the decision below does not conflict with *McCullough* v. *United States*, 462 F. 2d 588 (C.A. 5). There, the court rejected the government's imposition of Section 6672 liability upon a corporate officer who assumed his position after the taxes in question had been withheld and continued to serve in that capacity during a period in which certain funds came into the corporation's possession that would have been sufficient to discharge unpaid withholding taxes for prior periods. But as the court below correctly recognized (Pet. App. A9), *McCullough* turned on the fact "that it was clear from the evidence that the continued operation for approximately six months of the tenure of R. F. McCullough was at the will of a large factoring company which had security instruments covering substantially all the assets of the corporation and advanced funds for the operation only as itemized by specific voucher" (462 F. 2d at 590).

Unlike this case, the officer in *McCullough* had no unencumbered funds available to pay the withheld taxes. The Fifth Circuit specifically left open the question resolved against the officer in this case, *viz.*, the liability of a person who becomes an officer responsible for the payment of previously withheld unpaid withholding taxes when the corporation subsequently comes into possession of funds from which the officer could pay such taxes but fails to do so and instead disburses the funds for other purposes (*id.* at 590). *McCullough* held "only that the government did not prove facts sufficient to establish the existence of such a [trust] fund at a time when R. F. McCullough was the managing official" (*ibid.*). Here, in marked contrast, the court of appeals stated that "The evidence is undisputed that Tas-Tee Catering had in its possession during the period of

* * * [petitioner's] control large sums of money which it used to pay debts and operating expenses" (Pet. App. A9).[2]

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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[2]Petitioner also argues (Pet. 8) that the Fifth Circuit in *McCullough* stated that Section 6672 "is to be read in the conjunctive, whereas the Sixth Circuit has said the opposite." In petitioner's view, the statutory language—"person required to collect, truthfully account for, and pay over"—means that personal liability for withholding taxes can only be imposed on an officer who fails to perform each of the three enumerated functions, *viz.*, collection, accounting and payment. While we submit that Section 6672 is more properly read to reach an officer who fails to perform *any* one of the three functions, it was not necessary for the court below to address the correctness of the Fifth Circuit's dictum in *McCullough* because the decision in that case turned on the state of the evidence. At all events, the Fifth Circuit will shortly hear argument in *Brown* v. *United States* v. *Stifler* (No. 76-2381), which presents the question whether Section 6672 is applicable to a situation that is comparable to this case.

*The Solicitor General is disqualified in this case.

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